

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

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Statutory Review of the System)	
For Regulating Rates and Classes)	Docket No. RM2017-3
For Market Dominant Products)	
_____)	

Reply Comments of Discover Financial Services
March 30, 2018

Discover Financial Services (DFS) submits these Comments in response to the Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products (Notice), released in this Docket as Order 4258 on December 1, 2017. In Discover's Initial Comments, DFS made several points. In reviewing the Comments, Discover finds a great deal of support for its views.

I.
Digital Competition

First, the Commission's proposed changes do not allow the Postal Service to address in a streamlined fashion one of the main challenges to its financial health—the diversion of marketing dollars from the mail channel to digital marketing channels. This diversion is gaining strength throughout the marketing world and can no longer be ignored. The Commission needs to create a rate structure that allows the Postal Service to respond to competition rather than continue to hinder it. The future is going to demand more pricing flexibility from the Postal Service and it is going to demand it

from where the significant money is—market-dominant products. See generally ABA Comments at 1, 5; Hartford Comments at 1-2; Netflix at 4-9.

In 2014, we had the example of an NSA presented to the Commission by the Postal Service and DFS, designed to head off a diversion of \$100 million from mail to digital. Although this is exactly what the PAEA intended NSAs to do, the Commission decided not to accept the NSA. As a result, the Postal Service lost more than \$100 million in revenue from Discover.

II. Responsibility for the Postal Service's Financial Position

It is the prefunding of retiree health care benefits that is responsible for the poor financial health of the Postal Service, and not the ratemaking system, which has worked fairly well. Yet the Commission's proposed rulemaking does not acknowledge that the prefunding is the causal root of the problem, and that the problem is so large that any redesign of the ratemaking system will not fix the Postal Service's financial problems. Raising rates high enough to cover the prefunding shortfall would drive so much mail out of the postal system that, inevitability, volumes and revenues would decline so low that the volumes and revenues left would not be sufficient to support the postal distribution network. E.g. Calmark at 2, MMA at 3-5.

As the Commission recognizes, only Congress can (and eventually must) provide relief in this area. The ratemaking system functions well for its intended purpose and changing it will not have an appreciable effect on the Postal Services finances. In fact, the Commission's proposed rate making structure could easily provide a convenient excuse for Congress to do nothing about alleviating the prefunding burden. The

Commission should not pretend that the proposal in this Docket will lead the Postal Service to financial stability. See *e.g.*, SIIA at 11-12; ABA at 2-5, 6-8.

With this in mind, DFS urged the Commission in its initial Comments to adopt as its primary guide in this matter, the medical tenant, “first do no harm.” This recommendation has been echoed by a number of others. See, *e.g.*, Calmark at 2; SIIA at 12; AB Data at 2; News Media Alliance at 3-7; Schreur Printing and Mailing at 3; Tribune Direct at 2.

III. Regulatory Complexity

DFS has expressed its strong concurrence with Commissioner Hammond’s point that this proposal overlays questionable regulatory complexity on the ratemaking process. The Postal Service needs more rate streamlining and more rate simplicity, not less. Support for this view permeates most of the Comments that were filed. This is because many, if not most, postal products—both market dominant and competitive—compete for the same dollar with alternative communication channels, digital and non-digital. The less flexibility the Postal Service has in rates, and the less streamlined its processes, the weaker its competitive position. The Postal Service needs to be able to respond to competitors’ pricing changes in hours and days, not in days and months. This is particularly true of market dominant marketing products. Yet this proposal provides no streamlined mechanism for the Postal Service to nimbly challenge its competition. As DFS has said in the past, in the real world, marketing mail is competitive mail. This docket provides a good opportunity for the Commission to move

marketing mail from the market-dominant side of the Postal Service to the competitive side, where it now belongs.

V.
Effect of Exigent Surcharges.

Finally, DFS wishes to address the point Commissioner Hammond made in his dissent about exigent surcharges: “I note that the exigent surcharges that were in effect from 2014 to 2016 appear not to result in any additional volume loss. Therefore, they may serve as a useful starting point for analysis.” Hammond Dissent at 2.

First, Discover’s mail marketing volume and revenue did not remain constant during the 2014 to 2016 time frame, but dropped precipitously. Second, marketing budgets during that time were still responding to the Great Recession. For many other companies, advertising can be the first casualty of a recession and the last to come back after a recession, although marketing experts suggest this is not a wise strategy. Financial pressures may take precedence over marketing considerations during periods of financial stress. As a result, in 2014 to 2016, many other companies’ marketing was still climbing out of the recession and their response to higher postal prices could have been somewhat duller than normal.

Third, volume responses to higher postal prices is not immediate. Moving from mail marketing to digital marketing requires a certain digital expertise which usually requires new hires, a digital infrastructure with new capital expenditures, plus a digital marketing plan that requires one, if not more, years to develop. Even a company like Discover, whose digital expertise was high, requires lead time for digital planning. See MMA et al at 2.

Conclusion

As a final comment, Netflix makes the point that the Performance Incentive Mechanism (PIM) conflicts with basic price cap principles and is unworkable. Netflix argues that it should be removed from the plan. Netflix at 3,19—24. See Hammond at 2.

DFS agrees.

Respectfully submitted,

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